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WASHINGTON, D.C. 20006-3458
(202) 659-9750

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*ADMITTED IN CALIFORNIA ONLY

ALAN RAYWID
(1930-1991)

OF COUNSEL
FRANCES J. CHETWYND
ELLEN S. DEUTSCH

FACSIMILE
(202) 452-0067

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May 17, 1999

Hand Delivered
Ms. Magalie Roman Salas
Office of the Secretary
Federal Communications Commission
445 Twelfth Street, S.W.
Room TW-A325
Washington, D.C. 20554

Re: GTE Petition for Declaratory Ruling
CC Docket No. 99-143

Dear Secretary Salas:

Enclosed please find an original and seven (7) copies of the Comments of Global NAPs Inc. in the above-referenced proceeding. The attached document was also filed electronically via the ECFS system.

Please return a filed-stamped copy of this letter to me in the enclosed stamped, self-addressed envelope.

Very truly yours,

Christopher W. Savage

cc: Attached Service List

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Before the
Federal Communications Commission DOCKET FILE COPY ORIGINAL
Washington, D.C. 20554

In the Matter of Request for Declaratory Ruling Regarding the Use of Section 252(i) to Opt into Provisions Containing Non-Cost-Based Rate	CC Docket No. 99-143

COMMENTS OF GLOBAL NAPS, INC.

Christopher W. Savage
COLE, RAYWID & BRAVERMAN, L.L.P.
1919 Pennsylvania Avenue, N.W., Suite 200
Washington, D.C. 20006
202-659-9750

William J. Rooney, Jr
General Counsel, Global NAPs Inc.
Ten Merrymount Road
Quincy, MA 02169
617-507-5111

Date: May 17, 1999

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Before the
Federal Communications Commission
Washington, D.C. 20554

In the Matter of Request for Declaratory Ruling Regarding the Use of Section 252(i) to Opt into Provisions Containing Non-Cost-Based Rate	CC Docket No. 99-143

COMMENTS OF GLOBAL NAPS, INC.

1. Introduction and Summary.

GTE's Petition[1] is the latest attempt by an incumbent local exchange carrier ("ILEC") to recruit the Commission into a relentless war of attrition against Internet Service Providers ("ISPs") and the competitive local exchange carriers ("CLECs") who are trying to meet their telecommunications needs. GTE's specific gambit is to distort the pro-competitive nondiscrimination requirements of the Act into a means for limiting the competitive damage that CLECs can do to ILECs' entrenched monopolistic control of the local exchange, while imposing a form of cost-based rate regulation on CLECs to boot. The Commission should reject this pernicious, anticompetitive proposal.

GTE's fundamental claim — that Section 252(i) does not or should not apply to terms of interconnection agreements that are not cost-based — is wrong. It is true that costs can change over time, so that a price term that was established in accordance with the standards of Section 252(d) might need to be updated from time to time. Nothing in the Act, however, requires a ***negotiated*** price term to be cost-based. If an ILEC has agreed to pay a CLEC a particular rate, that same rate must be made available to any other CLEC for performing the same

[1] GTE Petition for Declaratory Ruling, CC Docket No. 99-143 (filed April 13, 1999) ("Petition").

function. Otherwise the CLEC with the agreement in question will have an unfair advantage over other CLECs with which it competes.

GTE is particularly concerned about CLECs who might be more efficient at call termination than GTE itself is. It therefore launches a collateral attack on the Commission's requirement of symmetrical rates by suggesting that if a call termination rate based on ***GTE's*** costs overcompensates a ***CLEC*** for terminating calls, then GTE should be permitted to prevent that CLEC from opting into an agreement containing that term. GTE, in short, wants the Commission to endorse the destruction of entreprenurship. If GTE has agreed to pay (say) $0.01/minute for call termination, it cannot abide the prospect that a CLEC might be able to perform that function at a lower cost, thereby (as entrepreneurs are wont to do) earning profits from its activities. GTE wants the Commission to squelch this unseemly capitalistic behavior.

Finally, GTE reserves a special circle in regulatory purgatory for CLECs that are not merely more efficient, but instead have had the temerity to deploy innovative technologies and equipment architectures for handling incoming calls to ISPs. Apparently the technologies that these CLECs have deployed are especially good at sorting out which incoming calls go to which ISPs. In GTE's view, therefore, these CLECs should be specifically banned from opting into even a cost-based call termination rate (using GTE's own costs as the benchmark). Presumably these entrepreneurs would be faced with the prospect of CLEC-specific cost analyses to establish a regulatory limit on the rewards from their entrepreneurship.

The Commission should reject GTE's proposals in their entirety.

The remainder of these Comments is organized as follows. Section 2 reviews the purpose and operation of the Act's non-discrimination provisions, which GTE warps beyond all recognition. Section 3 explains why — contrary to GTE's claim — the *Declaratory Ruling* cannot be read to limit CLECs' rights to opt into agreements that provide for compensation for ISP-bound calls. Section 4 explains why Section 252(i) generally applies to non-cost-based rates in negotiated interconnection agreements, and why Commission Rule 51.809(b) already protects

ILECs from having to perform work for CLECs at below-cost rates when such protection is legitimately required. Finally, Section 5 explains why the fact that a CLEC might be more efficient than an ILEC provides no basis for an exemption from Section 252(i) or from the Commission's general rule requiring symmetrical compensation for call termination functions.

2. The Act's Non-Discrimination Provisions Are Intended To Protect CLECs, Not ILECs.

One way monopolists abuse their monopoly power is through discrimination. Favored customers or suppliers get special, preferential treatment; disfavored customers or suppliers are treated badly.[2] To prevent this behavior, public utility regulatory statutes, including the Communications Act, include non-discrimination requirements. *See, e.g.,* 47 U.S.C. § 202(a).

In the context of opening local telecommunications markets to competition, there are two types of potential discrimination to be concerned about. First is discrimination by the ILEC against disfavored carriers. This is banned in Sections 251(c)(2), 251(c)(3), 251(c)(4), and 251(c)(6), which require interconnection, access to unbundled elements, resale, and collocation arrangements to be nondiscriminatory. *See also* Section 252(d)(1)(A)(ii). These provisions come into play when an ILEC and a CLEC cannot agree on interconnection terms, and present the matter to a state commission for arbitration; the CLEC being (potentially) discriminated against can bring the matter to arbitration and receive an appropriate interconnection contract.

The second type of potential discrimination arises from the prospect that a CLEC might convince an ILEC to agree to terms that do not unfairly aid the ILEC, but that somehow give the CLEC an advantage over other CLECs. This problem would not arise with an arbitrated agreement, since state commissions must establish terms that comply with the nondiscrimination provisions cited above. Instead, it would arise in the case of negotiated agreements, which (under

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[2] The motivations for discrimination will vary from case to case. Traditionally, customers that had some possible alternative to using the monopolist's services received preferential rates, while truly "captive" customers received unreasonably high rates. More subtle arrangements, such as giving preferential treatment to firms that provide unrelated benefits (such as dealing with the monopolist's unregulated affiliate in some manner) are also possible.

Section 252(a)(1)) need not comply with those provisions. This potential problem is addressed in Section 252(e)(2)(A)(i), which requires state commissions to reject a negotiated agreement that "discriminates against a telecommunications carrier not a party" to it.

An added protection in each case is Section 252(i). Section 252(i) allows any CLEC to take advantage of the terms of any approved agreement to which the ILEC is a party. As a result, if some type of discriminatory arrangement slips through the cracks and is embodied in an approved interconnection agreement (whether negotiated or arbitrated), discrimination is ***still*** avoided, because under 252(i) — at least in theory — any CLEC can demand exactly the same terms and conditions the ILEC has agreed to with any other CLEC.

In fact, Section 252(i) goes even farther. By establishing that any CLEC may get the same deal that any other CLEC got, Section 252(i) expedites market entry by allowing the latest CLEC entrants to avoid the time and expense of negotiating (and perhaps arbitrating) a hand-crafted interconnection agreement if an acceptable agreement has already been approved by the relevant state commission. From this perspective, in any ILEC/CLEC negotiation, the terms contained in existing interconnection agreements are "on the table" as a matter of law, so that the CLEC may at any time may demand those terms and get its business rolling.[3]

There is nothing unfair or unreasonable about this situation. Under Section 252(e)(2), state regulators review every interconnection agreement. A negotiated agreement will be approved if it is in the public interest and nondiscriminatory. If the state commission must arbitrate an agreement, it will establish one that is consistent with Sections 251 and 252. In either case, it would seem presumptively reasonable to make ***every*** approved interconnection

[3] Unfortunately, it has not always worked out this way in practice, as evidenced by Global NAPs' as-yet unsuccessful efforts to force Bell Atlantic simply to give Global NAPs the same deal that Bell Atlantic gave MFS Intelenet. These matters are currently before the Commission on petitions to preempt state regulatory authority in two different states.

agreement available to ***every*** CLEC, since every one will have a clean bill of statutory health.[4] Section 252(i) establishes exactly that presumption.

Under the "whole contract" rule imposed by the 8th Circuit (and in effect from October 1996 through January 1999), there was little need for any exception to this quintessential nondiscrimination requirement. If CLEC #2 would operate under ***exactly the same terms*** as CLEC #1, there would appear to be no legitimate basis for the ILEC to complain, no matter how complex or subtle the negotiating trade-offs embodied in the contract being opted into. Things are more complicated under "pick and choose." Theoretically, CLEC #10 could cobble together some provisions from the ILEC's agreement with CLEC #1, some from its agreement with CLEC #2, and so on. Such a cobbled-together agreement might somehow just not work right. This potential problem, however, is addressed by 47 C.F.R. § 51.809, which allows the ILEC to prove that CLEC #10 should not get some particular provision, either because it is technically infeasible in the case of CLEC #10, or because the costs to the ILEC of providing it have increased so substantially that the ILEC is entitled to a higher price than in the original deal.[5]

GTE wants to turn these nondiscrimination provisions on their head. GTE's concern is not that the terms of an existing agreement might be unreasonable to the ILEC in light

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4 An ILEC, of course, may obtain judicial review of any state commission decision approving an agreement if that decision, in the ILEC's view, does not actually meet the relevant statutory standard.

5 If the 8th Circuit had not stayed Rule 51.809, there would be a wealth of precedent on how it should be interpreted. Case-by-case adjudication is particularly important in resolving the complex questions of discrimination that might arise under the terms of the Rule. For example, suppose three CLECs have agreements under which they can send calls to GTE at a per-minute rate of $0.005 per minute. Now suppose that a fourth CLEC wants to enter the market by opting into one of those agreements, but GTE is able to show that its costs have increased to (say) $0.007 per minute. Should the new CLEC be forced to operate at a competitive disadvantage to the original three CLECs (whose $0.005/minute rate would, presumably, remain unchanged for the duration of their contracts)? Or should the new CLEC get the same (now shown to be non-cost-based) rate for as long as the other CLECs can take advantage of it? Properly resolving these and similar questions will require a careful consideration of the facts of each case. Now that the process of case-by-case implementation of Rule 51.809 can finally begin, however, GTE is afraid of what the state commissions might do. It therefore wants this Commission to cut off the process before it starts and establish a regime in which GTE and other ILECs can practice massive discrimination against disfavored CLECs — particularly those with the temerity to try to meet the needs of ISPs.

of changes in the ILEC's costs or technology. To the contrary, GTE is concerned that if a CLEC is efficient enough in its operations or innovative enough in its technology, the CLEC might end up making too much money if it can operate under the same contractual terms as other CLECs. In GTE's hands, therefore, pro-competitive nondiscrimination requirements designed to protect CLECs against ILEC abuse would be converted into an excuse for imposing a form of cost-based regulation on particularly efficient and innovative CLECs. The Commission should recognize GTE's gambit for what it is and deny GTE's Petition.

3. Section 252(i) Applies To Agreements Providing For Compensation For ISP-Bound Calls.

GTE seeks a specific ruling that CLECs may not opt into agreements that have been ruled by state commissions to call for compensation for ISP-bound calls. *See* Petition at i, 3-4. GTE claims that such a ban is required by the *Declaratory Ruling*, but in fact the opposite is true. If a state commission has determined that an ILEC has agreed to pay compensation for ISP-bound calls — which the *Declaratory Ruling* specifically found may have occurred in many cases — then it would be the height of discrimination to say that one lucky CLEC may take advantage of that agreement, but other CLECs may not.

GTE complains that it never really agreed to pay compensation for ISP-bound calls, but that misguided state regulators have held that it did. *See* Petition at i, 7. GTE, therefore, wants the Commission to rescue it from the damage caused by these state rulings, by preventing CLECs from opting into the contracts that provide for such compensation.

This is nonsense. If GTE thinks the state commissions got it wrong, it can take them to federal court (and, indeed, is probably doing so). From that perspective, GTE's Petition here is simply a collateral attack on state decisions with which it disagrees.

But GTE is also wrong on the merits. GTE knows full well that for the last fifteen years the Commission's rules have required that ISPs be allowed to subscribe to local exchange services like any other business customer, precisely for the purpose of ensuring that they may receive local calls from the end users who subscribe to the ISPs' services. The result has been that since 1983, calls to ISPs have been treated as local calls, even though over that same period the Commission has held that the calls at issue were "really" interstate. In these circumstances, the underlying industry understanding — the regulatory context within which negotiations would take place — was clearly that ISP-bound calls were, or at least were to be "treated as," local.[6]

As the Commission has explicitly found, this historical and regulatory context provides a logical basis for interpreting interconnection agreements:

> [A]lthough recognizing that it was interstate access, the Commission has treated ISP-bound traffic as though it were local. In addition, incumbent LECs have characterized expenses and revenues associated with ISP-bound traffic as intrastate for separations purposes. ... Against this backdrop ... parties entering into interconnection agreements may reasonably have agreed ... that [ISP-bound] traffic should be treated in the same manner as local traffic. When [determining] whether the parties so agreed, state commissions [may] consider all the relevant facts, including [1] the negotiation of the agreements in the context of this Commission's longstanding policy of treating this traffic as local, and [2] the conduct of the parties pursuant to those agreements. For example, it may be appropriate for state commissions to consider [3] whether incumbent LECs serving [ISPs] have done so out of intrastate or interstate tariffs; [4] whether revenues associated with those services were counted as intrastate or interstate revenues; [5] whether ... incumbent LECs or CLECs made any effort to meter this traffic or otherwise segregate it from local traffic, particularly for the purpose of billing one another for reciprocal compensation; [6] whether, in jurisdictions where incumbent LECs bill their end users by message units, [they] have included calls to ISPs in local telephone charges; and [7] whether, if ISP traffic is not treated as local and subject to reciprocal compensation, incumbent LECs and CLECs would be compensated for this traffic.

Declaratory Ruling at ¶¶ 23-24. It seems quite likely that applying these factors to the vast majority of interconnection agreements will lead to the conclusion that the parties' intended to

6 This history is reviewed in Implementation of the Local Competition Provisions in the Telecommunications Act of 1996; Inter-Carrier Compensation for ISP-Bound Traffic, *Declaratory Ruling in CC Docket No. 96-98 and Notice of Proposed Rulemaking in CC Docket No. 99-68,* CC Docket Nos. 96-98 & 99-68 (rel. February 26, 1999) ("*Declaratory Ruling*").

treat ISP-bound calls as local. Indeed, this is exactly what appears to be occurring in the wake of the issuance of the *Declaratory Ruling*.[7]

GTE may now, in retrospect, wish that it had written its interconnection agreements differently. But such sentiments, however sincere, provide no basis for limiting CLECs' rights or ILECs' duties under Section 252(i). Stripped to its essentials, what GTE wants is a rule under which it must offer the terms of approved interconnection agreements to any CLEC that requests those terms — except when it doesn't want to. A slightly different take on GTE's goal is that it wants a ruling that any time it engages in litigation over what a disputed contract term means, and loses, it can pretend that it won for purposes of Section 252(i).

In fact, unless CLECs are permitted to exercise their Section 252(i) rights with respect to contract terms that the ILEC wishes it could deny them (for whatever reason), the entire statutory provision becomes a nullity. If the ILEC has no objection to allowing one CLEC to operate under the same terms already embodied in a contract with another CLEC, then there will be no dispute between the parties over those terms. The entire point of the explicit statutory nondiscrimination obligation is to give new CLECs the power to ***force*** the ILEC to provide the same terms provided to an existing CLEC, even when — indeed, especially when — the ILEC does not want to do so.

This logic fully applies to the treatment of ISP-bound calls as "local." As Global NAPs has detailed elsewhere, ILECs have historically failed to meet the sophisticated telecommunications needs of ISPs.[8] This creates an opportunity for "ISP-friendly" CLECs to meet those needs. Under the "access charge exemption," however, it is economically impossible

[7] As of the date of this filing, state commissions acting in light of the *Declaratory Ruling* have concluded that interconnection agreements indeed contemplated treating ISP-bound calls as local in Delaware, Florida, Alabama, Ohio, Nevada, Washington, Oregon and Hawaii. In addition, an arbitrator in California has reached the same result, and no state regulator has concluded the contrary. (One state, Missouri, has concluded that it will not decide the issue but will, instead, await the outcome of the Commission's rulemaking proceeding on this issue.)

[8] *See* Comments of Global NAPs, Inc. in Docket Nos. 96-98 & 99-68 (April 12, 1999) ("Global NAPs Comments"), especially "Statement of Fred Goldstein."

for a CLEC to charge ISPs for the costs incurred in switching incoming calls to the appropriate ISP line, because that would make the CLEC's service much more expensive than otherwise similar ILEC service.[9] As a result, the only way a CLEC can compete for the business of ISPs is if the costs of switching incoming calls are recovered from the originating LEC.

In practical terms, this means that granting GTE's Petition would limit competition in the market for serving ISPs' telecommunications needs to those CLECs that already have agreements that provide for compensation for ISP-bound calls. Those CLECs could participate in that rapidly growing market knowing that they would receive compensation from the ILEC for the work they do on behalf of the ILEC's customers (*i.e.*, the ones calling the ISPs). Upstarts such as Global NAPs, Focal and others who believe they can serve this market efficiently, but who were not "first to market" in a particular area, however, would be frozen out. There is no conceivable basis in law or policy for such a blatantly anticompetitive result.

In sum, then, where a state commission has determined that an interconnection agreement between an ILEC and one CLEC provides for compensation for ISP-bound calls, it is logical, economically appropriate, and legally sound to require the ILEC to extend that same provision to other CLECs. The force of this conclusion is not weakened when the ILEC can truthfully state that it does not want to extend the provision to other CLECs. To the contrary, that is the only time that the legal force of Section 252(i) (and the other non-discrimination provisions of the Act) come into play at all.

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[9] It also makes no policy or economic sense to charge the ISP for the costs of switching incoming calls. When an end user calls an ISP, the end user, not the ISP, is the cost-causer with respect to all the switching and transport functions needed to get the call from the end user's location to the ISP's line or trunk port on the terminating switch. (The costs of the port and the loop facilities associated with the ISP's line are caused by the ISP.) For this reason, among others, the access charge exemption is entirely economically sound policy. *See* Global NAPs Comments, *supra*, and Reply Comments of Global NAPs, Inc. in Docket Nos. 96-98 & 99-68 (April 26, 1999) ("Global NAPs Reply").

4. Section 252(i) Applies To Non-Cost-Based Rates.

As part of its effort to deny CLECs the right to compete for the business of ISPs, GTE notes that some interconnection agreements contain non-cost-based rates, and argues that the presence of such rates in an agreement should render Section 252(i) inapplicable. Petition at 5, 7-9. There is no policy or legal basis for such a conclusion.

GTE's argument in this regard actually has two different aspects. First is the plainly false premise that the Act contemplates that only cost-based rates will be included in interconnection agreements. Second is a collateral attack on the Commission's sound rule requiring symmetry, *i.e.,* that an ILEC pay a CLEC for terminating traffic the same amount that the CLEC is obliged under the contract to pay the ILEC, when the CLEC is more efficient than the ILEC. The first is addressed below; the second is addressed in Section 5, *infra*

Sections 251 and 252 establish a regime where the preferred way to reach interconnection agreements is through negotiation. Sections 251(b) and (c) set out a number of duties for both ILECs and CLECs, and Section 252(d) provides some specific guidance on how particular functions must be priced if either party insists on the fulfillment of those duties. But Section 252(a)(1) makes clear that if an ILEC and a CLEC can agree to interconnection terms that do not actually fulfill their respective duties, that is perfectly acceptable.

The legal standard under which state commissions review agreements reflects this fact by varying radically between the case of a negotiated agreement and the case of an arbitrated agreement. If the parties cannot agree to interconnection terms, then the state commission is required to impose terms that comport with the requirements of the Act, including the requirement that rates be cost-based. *See* Section 252(e)(2)(B). But if the parties can agree, the law establishes a strong presumption in favor of approval. Under Section 252(e)(2)(A), a negotiated agreement may only be disapproved if it is not in the public interest or if approval would result in discrimination against carriers not parties to it.

Nothing in Section 252(e)(2)(A) requires that the rates in a negotiated agreement be cost-based. If the "real" cost of terminating a minute of traffic is (say) $0.003, but the parties agree for some reason to accept a higher or lower figure, nothing in Section 252(e)(2)(A) suggests that such an agreement is not in the public interest or that it would be discriminatory — as long as the same terms are made available to other CLECs.

Note that contracting parties could reasonably agree to include non-cost-based rates in a contract. First, a non-cost-based rate might reflect the fact that a party has accepted obligations not required by the Act. For example, while not primarily a matter of concern to GTE, some RBOC interconnection agreements expressly oblige the CLEC to undertake, over time, to serve both business and residence customers. One possible way to recognize the existence of such obligations is to include price terms that over-compensate the party bearing them.[10] Another scenario that could lead to non-cost-based rates is different ILEC and CLEC assessments of the market. Suppose that the ILEC and the CLEC each firmly believes that it will be a net receiver of traffic. One of them will be wrong; but in negotiations, both of them will want to establish a relatively high call termination rate.

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[10] Nothing in the Act requires a CLEC to serve residence customers. Moreover, decades of experience shows that serving residence customers is not as profitable as serving business customers. This would probably be true even in states that have established a competitively neutral universal service funding mechanism under Section 254(f), and is plainly true if — as is the case, to Global NAPs' knowledge, essentially everywhere — no such state-level mechanism exists. For this reason, the impact of a requirement that a CLEC serve residence customers is that the CLEC's profits will be lower than they otherwise would be, while the RBOC will be better positioned to seek interLATA relief under Section 271. It would not be irrational for contracting parties to take the lower CLEC profits — and the benefit to the RBOC — into account when establishing the overall economics of an interconnection agreement.

In this regard, some ILECs — in Global NAPs' experience, notably Bell Atlantic — appear to believe that unless a CLEC serves the entire, broad market of business and residence customers, the CLEC is either not a LEC at all, or is, at best, some sort of second-class citizen in the world of telecommunications carriers. This is wrong as a matter of the regulatory history of the telecommunications industry and under the statute. As to history, the Commission will recall that MCI was once a specialized provider of interstate private line microwave services, and MFS was once a provider of fiber-based interstate special access circuits. As to the statute, it is clear that under Section 214(e), in the normal case a CLEC may elect either to undertake to provide "universal service" or not.

It follows that if a non-cost-based rate has been negotiated between an ILEC and a CLEC, that fact is no reason to deny exactly the same rate to another CLEC. Negotiated rates do not have to be cost-based. Granting GTE's Petition, therefore, would logically lead to a rule under which CLECs may exercise Section 252(i) "opt in" rights with respect to arbitrated contracts, but not negotiated contracts. But this would gut the effect of the nondiscrimination obligation, because arbitrated terms, established by state commissions, are not likely to contain discriminatory elements. The entire purpose of Section 252(i) (and the related non-discrimination provisions in the various subsections of Section 251(c)) is precisely to ***prevent*** an ILEC from voluntarily agreeing to a special deal that would be available only to one or a few CLECs.

Rule 51.809 is not to the contrary. Depending on the term (in years) of a particular interconnection agreement, it is possible that even an arbitrated price for some function — cost-based at the time it takes effect — could become non-cost-based over time. It therefore makes sense for the ILEC to be able to object to providing some function for a rate that over time, and due to rising costs, might have become too low. Rule 51.809(b)(1) directly addresses this problem by permitting the ILEC to prove that "the costs of providing a particular [function] to the requesting [CLEC] are ***greater than*** the costs of providing it to" the CLEC that was the original party to the agreement.

Two features of this rule are particularly relevant here. First, the rule says nothing about costs to the CLEC of functions that a CLEC provides to an ILEC. The rule, therefore, is on its face inapplicable to the situation addressed by GTE's Petition.

Second, the rule says nothing about prices or the relationship of price to cost. If an ILEC's call termination ***costs*** at the time of a negotiated agreement were (say) $0.004 per minute, but the agreement provided for a call termination ***price*** of (say) $0.05 per minute, the ILEC may be able to get a higher call termination rate in a later agreement if it can show that its ***costs*** have actually increased to $0.006 per minute. But if the ILEC's call termination costs have not increased, it cannot use Rule 51.809 to avoid its Section 252(i) duties simply because of a mismatch between costs and prices in the original, negotiated agreement.[11]

Some ILECs have argued that they may avoid their Section 252(i) obligations under Rule 51.809(b)(1) if the CLEC seeking to opt into an agreement will likely receive a greater volume of calls than the ILEC anticipated sending to the CLEC with whom it originally negotiated an interconnection agreement. They argue that they will incur greater call termination liabilities under a contract with the new CLEC, and that this fact triggers Rule 51.809(b)(1). This, of course, is nonsense. (It is not clear whether GTE intends to make this argument or not.) Rule 51.809(b)(1) applies when the ILEC is "providing a particular interconnection, service, or element" to the CLEC. But when the ILEC sends traffic to a CLEC, the ***CLEC*** is the one "providing [the] interconnection, service or element." In addition, the point of the rule is to protect the ILEC from increases in the underlying ***unit cost*** of providing some function, not to allow it to discriminate against (or in favor of) high-volume, as opposed to low-volume, CLECs.

Consequently, if an ILEC voluntarily agrees to pay an above-cost rate, or to receive a below-cost rate, that rate must be available to all CLECs, non-cost-based though it may be. Any other interpretation of Section 252(i) would be an open invitation to ILECs to enter into special, discriminatory deals with one or more favored CLECs, and then cry "non-cost-based rate!" when another CLEC tries to take advantage of the same deal. On the other hand, if a call termination or other rate has been arbitrated, that rate will ***be*** cost-based, at least to the best of the state commission's ability to determine cost. So in agreements where the rate for call termination is an arbitrated rate, GTE's issue will only rarely arise, and when it does, Rule 51.809(b)(1) will provide all the protection the ILECs need.

[11] In an arbitrated agreement, the price will have been set at the state commission's determination of the ILEC's costs, so any increase in costs will logically justify some increase in the rate under Rule 51.809(b). Even so, these questions must be handled carefully in each case, so that CLECs are not disadvantaged relative to other CLECs. *See* note 5, *supra*.

5. GTE's Proposal Is A Collateral Attack On The Commission's Requirement Of Symmetrical Call Termination Rates.

GTE is particularly concerned that some CLECs may be much more efficient than GTE is itself in performing call termination functions. *See* Petition at 6-10. This amounts to an assertion that while GTE might have call termination costs of (say) \$0.005/minute, a particular CLEC might have call termination costs of only (say) \$0.002/minute. Under the Commission's rules requiring generally symmetrical call termination rates, however (Rule 51.711), the efficient CLEC would get paid \$0.005/minute for call termination. GTE's Petition, in effect, asks the Commission to modify the general rule requiring symmetrical rates to ensure that these particularly efficient CLECs do not make too much money.

At the outset, it bears emphasis that GTE's premise of a wildly efficient CLEC is far from likely to exist in the real world. Even a very efficient CLEC will lack an ILEC's economies of scale, and in this capital-intensive business there is no question that entrepreneurial CLECs face vastly higher capital costs than long-established, monolithic, monopolistic ILECs. This means that CLECs with operations that appear to be similar to the ILEC's will actually be incurring much higher costs than the ILEC incurs.[12]

But suppose that GTE's premise is right, that the CLEC is actually more efficient than the ILEC in terms of actual operations today. That does not provide a reason to deny the CLEC the benefit of its Section 252(i) rights.

First, for the reasons described in the preceding section, if the non-cost-based rate was established by negotiation as opposed to arbitration, the inquiry should be at an end.

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[12] Suppose that the appropriate depreciation life and cost of capital for an ILEC switch are 15 years and 10%, respectively. The monthly levelized capital cost (depreciation and return on investment) on a \$2.5 million switch under these assumptions is approximately \$26,900. Now suppose that for an entrepreneurial CLEC, the appropriate depreciation life is 5 years and money from venture capitalists can only be had at a cost of 30%. The CLEC's monthly levelized capital cost ***for the same switch*** would be approximately \$80,900 — more than three times as much. A lack of CLEC economies of scale in operations and a likely inability to get preferred prices from switch vendors would only heighten the CLEC's cost disadvantage.

Negotiated rates need not be cost based, and requiring that they be available to all CLECs prevents ILECs from entering into discriminatory deals with favored entities.

Second, even if the rate in question was arbitrated, not only does the statute not require precision in determining call termination costs, it positively rejects any effort to be precise. Thus, Section 252(d)(2)(A)(ii) requires only that call termination rates be set at "a reasonable approximation" of the costs of terminating calls, and Section 252(d)(2)(B)(ii) specifically forbids proceedings that would establish such costs "with particularity." So only ***very*** substantial cost differences could possibly justify limiting a CLEC's Section 252(i) rights. One could reasonably conclude that if the ILEC's call termination costs are within (say) a penny per minute of the CLEC's costs, the approximation is "reasonable" enough.

Third, even if it might be true in some cases that the cost difference is so great that the ILEC's costs cannot be viewed as a "reasonable approximation" of the CLEC's costs, regulators must impose a heavy burden on ILECs to show that such a situation actually exists. At a minimum, the ILEC should be required to present a study of the costs of a hypothetical CLEC using presently available technology that shows a truly substantial cost advantage for the CLEC. Review of such a study should be completed before a regulator should even entertain a claim that a particular CLEC should be denied its Section 252(i) rights. Unless the ILEC's procedural burden is at least this high, Section 252(i) will become a nullity as every CLEC is challenged to prove that it is no more efficient than the ILEC before it will be permitted to opt into an existing contract. Here, GTE has not remotely met its burden, and has not remotely justified the general moratorium on opting into contracts calling for compensation for ISP-bound traffic that is its true objective.[13]

Fourth, under the TELRIC standard, it is hard to imagine that such cost differences would ever exist over an appropriately defined "long run." As noted above, if the ILEC and the

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[13] Note that if the Commission determines in its ongoing rulemaking regarding inter-carrier compensation for ISP-bound calls that such compensation is governed by Section 201(a) (as opposed to Sections 251 and 252, it is free to establish any compensation scheme that is "just and reasonable." The specific requirements of Section 252(d) would not apply to such a regime.

CLEC are using the same technology, the ILEC's economies of scale, stable operating environment and low capital costs dictate that the ILEC's costs will be lower than the CLECs. But if the CLEC has deployed some innovative technology that radically lowers its costs, then it would appear that on a ***forward-looking*** basis, the ILEC should be able to implement that same technology and lower its own costs. In these circumstances, an ILEC complaint that CLECs with whom it interconnects are "too efficient" should set off regulatory alarm bells, because what that really means is that the ILEC's own supposedly "cost-based" rates are too high.[14]

From this perspective, what GTE is really complaining about is the problem of "regulatory lag" arising from the prospect of CLECs using new, efficient technology while getting paid an arbitrated call termination rate based on the use of old, inefficient technology. As the Commission knows from its experience with price cap regulation, however, some degree of "regulatory lag" in aligning carriers' costs with the prices they charge is essential to providing an incentive to be efficient. From this perspective, then, what GTE really wants is a regime under which CLECs — particularly efficient, innovative CLECs — are subjected to a form of cost-based rate regulation before they are allowed into the market.

6. Conclusion.

GTE's Petition is totally without merit. ILECs are permitted under the law to agree to pay (or receive) non-cost-based rates. The need to enforce nondiscrimination provisions such as Section 252(i) is especially intense with regard to negotiated rates that have not been subjected to regulatory scrutiny under the terms of the Act; otherwise, the CLECs lucky enough to get the rates that the ILEC now wants to eliminate will have an utterly unwarranted market advantage over other CLECs.

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[14] In this regard, the Commission should not be misled by claims that CLECs specialize in serving particular customers while ILECs serve the broad market. These claims confuse the long run and the short run. In the short run, CLECs will of course specialize as they find niches where they can establish a foothold in the market before expanding into other areas. The fact that a CLEC tries to establish a toehold in the market by specializing on serving a particular market segment (such as ISPs) for one or a few years does not mean that the CLEC's ***long-run*** costs of call termination (or any other function) will be based on the costs of serving that specialized market segment.

With respect to arbitrated, supposedly cost-based rates, ILEC economies of scale and low capital costs make it quite unlikely in the real world that even an extremely efficient CLEC will have lower call termination costs than an ILEC. If such a CLEC exists, however, the statute does not require that the CLEC receive lower payments than the ILEC. Only if the CLEC is so much more efficient that the ILEC's costs cannot be viewed as a "reasonable approximation" of those of the CLEC would a lower rate be justified.

It is clearly a bad idea to give ILECs such an opportunity to delay market entry by the very CLECs who — by hypothesis — are among the most efficient providers in existence. At a minimum, therefore, an ILEC should be required to prove that such a CLEC could actually exist using currently available technology and CLEC-appropriate assumptions regarding matters such as depreciation, overhead, and capital costs. The ILEC should also be required to explain why the ILEC itself could not adopt the new, efficient technology, leading to a lowering of the call termination rates the ILEC itself receives when it terminates calls. Only then should a regulator even entertain a claim that a CLEC may not opt into an existing arbitrated call termination rate because it is too efficient.

For all these reasons, the Commission should deny GTE's Petition.

Respectfully submitted,

GLOBAL NAPS, INC.

By: ______________________

Christopher W. Savage
COLE, RAYWID & BRAVERMAN, L.L.P.
1919 Pennsylvania Avenue, N.W., Suite 200
Washington, D.C. 20006
202-659-9750

William J. Rooney, Jr
General Counsel, Global NAPs Inc.
Ten Merrymount Road
Quincy, MA 02169
617-507-5111

Date: May 17, 1999

CERTIFICATE OF SERVICE

I, Linda M. Blair, a secretary with the law firm of Cole, Raywid & Braverman, LLP, do hereby certify that copies of the foregoing have been sent via first class mail or hand delivery, this 17th day of May 1999, to the following:

Janice M. Myles*
Common Carrier Bureau
Federal Communications Commission
445 -12th Street, S.W., Room 5-C327
Washington, D.C. 20554

Ms. Magalie Roman Salas*
Office of the Secretary
Federal Communications Commission
445 -12th Street, S.W., Room TW-A325
Washington, D.C. 20554

International Transcription Services, Inc.*
1231 -20th Street, N.W.
Washington, D.C. 20036

Ms. Gail L. Policy
GTE Service Corporation
600 Hidden Ridge, MS HQ-E03J43
P.O. Box 152092
Irving, Texas 75015-2092

Gregory J. Vogt
Suzanne Yelen
Wiley, Rein & Fielding
1776 K Street, N.W.
Washington, D.C. 20006

Thomas C. Power*
Office of the Chairman
Federal Communications Commission
445 -12th Street, S.W., Room 8 B-201
Washington, D.C. 20554

Mr. Ed Krachmer*
Common Carrier Bureau
Federal Communications Commission
445 -12th Street, S.W., A-316
Washington, D.C. 20554

Ms. Tamra Preiss*
Common Carrier Bureau
Federal Communications Commission
445 -12th Street, S.W., Room 5-A232
Washington, D.C. 20554

Linda M. Blair

Linda M. Blair

*via hand delivery

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